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Financial Reporting Disclosure on Annual Reports of State Islamic Religious Councils in Malaysia

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ABSTRACT

The purpose of this paper is to examine the variation of the contents and the level of disclosure of the accounting information in the State Islamic Religious Councils' (SIRC) annual reports, in Malaysia. The matter under investigation is the review of the documentation related to the contents of accounting and reporting information of the annual reports. The secondary data of 13 annual reports from the 13 SIRCs in Malaysia have been examined. This is to evaluate the disclosure level of the selected information in those reports. The study employed a score of 100 point scale for each annual report, which comprises 13 disclosure items facilitated in the annual reports. The disclosure items in this study are a modification of the work by Pina and Torres. The study provides evidence that the contents of the SIRCs' vary from one to the other. It also indicates that the majority of the annual reports show a high level of disclosure of information.
KEYWORDS: Waqf, Accounting Information, Disclosure Level, Annual Reports.

INTRODUCTION

The nature of the sources of income and expenditure of the Islamic religious institutions such as the zakat, waqf and bait- al mal differ from other public, private or nonprofit institutions. The Islamic religious institutions were established within the Muslim community. The objectives of the institutions include religious and philantropic acts, charitable purposes, economic and alleviation of poverty, social welfare, education and health care services. The zakat institution has been established as an institution that organises the collection and redistribution of the zakat. It is a compulsory wealth tax to the Muslims with a fixed rate of 2.5% on the valuables and savings that are held for a year and above the basic minimum; known as nisab. The waqf institution, is another Islamic source of income, which has long been recognised as the oldest philanthropic and charitable institution in the civilization [2]. In performing the waqf, the owner repositions the ownership and benefit of the waqf assets to the trustee for the purpose of philantrophy and charity. The multi-dimensions of the philantrophic acts are substantial in providing free religious education, healthcare services, medical assistance, shelter and food, clothing and clean water for the Muslim community. Meanwhile, the bait- al mal is an Islamic institution which functions as the treasury department in the Islamic community or state. Nevertheless, in the Malaysian context, these institutions are under the jurisdiction of the State Islamic Religious Council (hereafter known as SIRC).

Malaysia comprises 14 states (Negeri Sembilan, Johor, Melaka, Selangor, Wilayah Persekutuan, Perak, Pulau Pinang, Perlis, Kedah, Pahang, Terengganu, Kelantan, Sabah and Sarawak), which make 14 SIRCs in Malaysia. The SIRCs in Malaysia abide to the financial reporting similar to the Federal and State Government of Malaysia which is based on the Financial Procedures Act 1957 (Revised 1972). The SIRCs are also bound to follow their State Islamic Administration Enactment Law issued by their states. The enactment slightly varies from one state to another. As the nature of the Islamic revenues obtained by SIRCs are totally from different sources, the SIRCs have issued supplementary accounting procedures and guidelines in order to facilitate the religious revenues requirement.

Motivation of Study

Several studies have been conducted by researchers pertaining to religious organisations. Most of the empirical studies were for the churches organisation, and very few for the Islamic organisation [3, 4, 5]. Their studies tend to gauge an understanding of the accounting and accountability in the Islamic religious organisation. Studies related to the financial reporting in Islamic religious organisations, that emphasise on the content of information and level of disclosure of the annual reports was neglected. Therefore, this motivates the researchers to conduct a study in

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relation to the disclosure of the annual reports which examines the contents and the level of disclosure of the annual reports in the Malaysian SIRCs.

LITERATURE REVIEW

Financial Reporting of SIRCs' Annual Reports

There are two contributing factors to the delay of the preparation of annual reports and late submission of the SIRCs' audit reports in Malaysia [3]. First, there is no proper written financial procedure to govern the financial administration and accounting system. Most of the SIRCs solely depend on the state religious enactment with certain modifications and treasury instructions or treasury circular from the Accountant's General Department (AGD). The second problem that arises is due to the lack of qualified and trained personal in the accounting field. During those periods (in the 1990s), most of the SIRCs did not have accountants and few of the organisations had executive accounting officers to handle the financial matters.

A recent study conducted by [5] indicates that the majority of the SIRCs do have accountants and assistant accountants. In their study, which focuses on the accounting practices on waqf by SIRCs in Malaysia, they discovered that the timeliness of the financial reports is improving. This is due to the utilisation of computerized accounting system which enhances their speed in preparing the annual reports. It can be concluded that through passage of the time and with the aid of Information and Communications Technology (ICT), the timeliness of the preparing of the annual reports in SIRCs have improved tremendously.

Financial Reporting and Disclosure

Financial disclosure is a set of financial reporting that shows a factor condition of balance sheet, income statement and notes to the accounts, which also incorporates the audit report [6]. On the other hand, in [7] widens the scope of the definition of financial reporting disclosure, which encompasses both financial and non-financial disclosure. The first initiative of measuring the financial reporting of the corporate disclosure by using weighted disclosure index was carried out by [8]. 31 informational items in relation to the independent variables such as assets size, number of stockholders, rate of return and method of trading shares had been analysed. The findings state that there are positive relationships between the corresponding items. In [9] included more independent variables such as listing status, "Big 8" versus "non Big 8" and earning margin which resulted in the indistinguishable findings. There are various studies that have been conducted by other researchers pertaining to the disclosure items field such as [10].

Initially, there were studies conducted to analyse the financial reporting disclosure in religious organisations. A very significant empirical study pertaining to the disclosure of financial reporting in religious organisations has been conducted by [11]. This study develops a disclosure index score for the annual reports of dioceses with respect to the accounting principles and reporting recommended by the American Institute of Certified Public Accountant (AICPA) and National Christian Commissioner's Board (NCCB). The study evaluates the disclosure practices of dioceses in relation to users' informational needs. It also examines the influence of four dioceses in determining the differences of the annual report disclosure among dioceses. The findings reveal that of the financial statements are publicly available. The disclosure of their report is similar to the reports of the "Big 8" and "non Big 8". It also indicates that the disclosure of dioceses in relation to Balance Sheet and Statement of Activity is in compliance with the Certified Public Accountants (CPA) requirement. Nevertheless, the study reveals low disclosure compliance with regard to Statement of Changes in Financial Position.

Development of Research Questions

There is a divergence approach in the study of financial reporting disclosure conducted by [1], as compared to the studies mentioned above. The main aim of study was to evaluate the relationship between the general objectives of the public accounting information and the disclosure in the annual reports. The secondary objective is to measure the quality and quantity of information disclosed. The focus is on the measurement and basis of accounting and it allows for the differences in the presentation format. The study selected secondary data from the 1992 annual reports published by the central administration from six countries (United States, Canada, New Zealand, Sweden and Spain).

The result espouses that public sector organisations in New Zealand have better quality of disclosure compared to others with regard to the relationship between the general objectives and the disclosure of accounting information. It reveals that Spain is the only country in the study that demonstrates the importance of budgetary information as compared to others while Sweden comes out as the country that proves the least importance in the budgetary system. The weaknesses in [1] are that they failed to distinguish between the mandatory disclosure items and voluntary disclosure items of the six countries in order to achieve their financial statement objectives. Secondly, as there are tremendous reforms and changes due to the new public management policy, whereby most of the countries have shifted from cash basis to accrual basis. Thus, it should be understood that the priorities and objectives of the particular countries changes in line with the reformation. In short, there exist a lacuna in accounting literature related to the content of accounting information and the level of disclosure items facilitated in the annual reports of the Islamic religious organisation. In view of the above literature, the researchers have developed two research questions, which are as follows.

Research Question 1: To what extent the contents of the accounting information in the SIRCs varied from each other?

Research Question 2: What is the level of disclosure of information facilitated in the annual reports of the SIRCs?

RESEARCH DESIGN AND METHODOLOGY

This study was conducted in 2002. To test the above research questions, secondary data i.e. annual reports of the SIRCs were obtained from the National Audit Department (NAD). For the purpose of the relevancy of the study, only those annual reports that had been audited and tabled in Parliament were taken into consideration. The assumption for this study are: 1) the data is not linear, 2) location and time is not significant and not a contributing factor in relation to the prior studies pertaining to the subject matter and 3) the study was undertaken with due respect to the Malaysian context and culture [12]. A reliability test was carried out to test the stability of the construction of the items [13]. This is because the items selected in the annual report are from the modification of [1]. Cronbach's Alpha was used to test the consistency level of the disclosure items. Due to the confidentiality, the SIRCs were anonymously known as SIRC A, B, C, D. E, F, G, H, I, J, K, L, M and N. The reliability test indicated a score of 0.9348. This demonstrated that the construction for the disclosure items was excellent.

Disclosure Index Development

The disclosure index was developed based on the study of [1] with certain modifications which analysed the relationship between the objectives of the governmental accounting system of six countries (the United States, Canada, Sweden, New Zealand, Australia and Spain). The work is identical to this study because both studies concentrate on the non-profit organisations. From the exhaustive lists of 26 financial disclosure items, 18 items were excluded and another 5 additional disclosure items were taken into consideration. The items were ignored because there were no such activities carried out by the SIRCs. The additional items were considered due to the relevancy of the items to the SIRCs annual reports. The researchers distinguished the level of disclosure by conceding the information facilitated in the annual reports with a score of one if the item was disclosed and a score of zero if the item was not disclosed. Later, all the scores obtained by the SIRCs were totalled up and divided with the total disclosure items in the annual reports and then multiplied by 100. It was summarized as follows.

Total disclosure items on the SIRCs annual reports = Total scores of the SIRCs 13 disclosure items X 100 (1)

The rationale for expressing the disclosure scores in percentage is that it will be much easier for the researchers to make comparison with the previous study because most of them employed the percentage method. The researchers define that the total scores of 60% and above will be considered as high level of disclosure. Scores obtained below 60% are considered as low level of disclosure.

RESULTS AND FINDINGS

In relation to research question 1, the contents of the annual reports indicate that historical cost is commonly used as their basis of accounting policy. The cash basis is practices due to its simplicity as compared to the accrual basis. There were SIRCs that applied a combination of the cash and the accrual basis method of accounting. SIRC E, for instance, uses the cash basis in the recognition of zakat and uses the accrual basis for other transactions. The presentation and contents of the annual reports vary from one SIRC to the other, thus SIRC J even includes its bank reconciliation statement as part of its annual report. SIRC K and D exclude the zakatable items as the collection and redistribution of zakat in those states were handled by the Zakat Central Collection. As such, the income and expenditure on zakāt do not appear in the income statement. In the case of SIRC D, the operations of collecting zakāt have been privatised. The private organisation has its own Board of Directors and committee members. All the SIRCs that disclose the zakat income reveal various types of zakat items such as the zakāt on income, savings, businesses, agricultural products, livestock, gold and minerals.

Table 1: Disclosure scores of SIRCs annual reports

State Islamic Religious Councils	Total Disclosure Scores (% age)
A	46
B	69
C	69
D	62
E	62
F	54
G	54
H	51
I	62
J	62
K	69
L	46
M	62
N	Not applicable

With reference to research question 2, Table 1 displays the disclosure scores of the annual reports of the SIRCs. The annual report for SIRC N is not available during the time of the study. The study ascertained that most of the SIRCs managed to disclose high level of disclosure items in their annual reports. Only the SIRCs L and M show otherwise. SIRC L demonstrates low disclosure items as this is due the accounting policies which did not require the SIRC L to disclose the physical assets. Similarly for the SIRC H, the annual report only discloses five disclosure items out of 13 disclosure items that have been listed by the researchers. The annual report did not exhibit comprehensive or detailed items for the annual reports.

The study suggests that the majority of the SIRCs demonstrated a high level of disclosure. This might be due to the absence of the standard requirement or guidelines or format on the information that should be disclosed in the annual reports. Thus, there were SIRCs that did not disclose all the items in the annual reports. It can be concluded that those SIRCs that did not score high in the disclosure items (i.e.SIRC A, F, G, H) might be due to the way the organisations presents the information facilitated in the annual reports. For example, SIRC H only discloses 4 out of 13 listed items, including the disclosure on the disclosure of the financial investment, revenues, expenses and accounting policies.

Table 2: Total disclosure items with relations to total disclosure scores

Selected accounting informations on the disclosure items	Total Disclosure Scores (%)
1. Disclosure of Physical Assets	69
2. Disclosure of Depreciation of Physical Assets	77
3. Disclosure of Financial Investment	85
4. Disclosure of Current Assets	85
5. Disclosure on Current Liabilities	62
6. Disclosure on Revenues	92
7. Disclosure on Expenses	92
8. Budgetary Information	0
9. Budgetary Modification Statement	0
10. Statement Application of Fund	0
11. Cash Flow Statement	92
12. Information on Long Term Investment	0
13. Accounting policies	92

Table 2 exhibits the total disclosure scores in relation to the disclosure items i.e. 13. First, it can be observed that a score of 92% was obtained from the disclosure on revenues, disclosure on expenses, cash flow and statement of accounting policies. Second, it can be observed that a score of 85% was obtained from the disclosure of financial investment and the disclosure of current assets. Third, it can be observed that a score of 77% was achieved from the disclosure of depreciation of physical assets. Lastly, it can be observed that 69% score was gained from disclosure of the physical assets. However, there were no such disclosure on the budgetary information, budgetary modification statement, statement application of fund and information on long-term investment.

The SIRCs disclosure scores on the physical assets are comparable to the disclosure for valuation of assets in Rowe and Giroux study (68%). Meanwhile, the SIRCs disclosure scores in the disclosure of policy of depreciation are higher than the work of Rowe and Giroux (55%). For the disclosure of income and expenditure, SIRCs annual reports outperformed the scores revealed. They reveal that larger charity organisations disclosed 28% of the income and expenditure accounts. Small and medium charities disclosed 7% of their income and expenditure accounts [14]. SIRCs and larger charities share similar interest in the disclosure of the cash flow statement. Both of them disclosed the cash flow statement, while for small and medium charity organisations, only 50% disclosed the cash flow statement.

In terms of depreciation, 88% of the larger charities capitalised and depreciated their fixed assets, 58% of the small and medium charities organisation depreciated their fixed assets whilst SIRCs indicate that they score 77% in the disclosure of the depreciation. As such, SIRCs differ in the methods of depreciation. One of the reasons why charity organisation did not disclose the depreciation on their fixed assets depreciated is due to the fact that they maintained the assets at their current condition [14].

Compared with [1] which stated that the disclosure scores ranged from 21% to 33%, none of the SIRCs revealed a disclosure on the budgetary information, budgetary modification statement, and sources on application of funds statement and information on long term investment projects. Previous study by [1] of six countries discovered that all the countries disclosed their budgetary information. New Zealand scored 50%, followed by Australia (47%) and the United States of America scored 42%. The budgetary information in the SIRCs might be treated as the sporadic information [4]. It is occasionally used for the management to inform on what other departments will be doing financially. The disclosure item is ignored in the annual report. Accordingly, though the majority of the SIRCs disclosed that their organisations had a long term investment, there was not much information pertaining to the particulars of the investments.

CONCLUSION

This study reports on the disclosure of the annual reports which examined the contents and the level of disclosure of the annual reports in the year 2000 (which had been audited and tabled in the Parliament) in the Malaysian SIRCs. By comparison, the disclosures of all the items in the SIRCs were higher as compared to the other religious organisations and other charitable organisations. The levels of disclosure of the SIRCs are higher as compared to all of the previous studies except for the budgetary information, statement of application of funds and information on the long term investment. Nevertheless, the disclosure items in the SIRCs varied due to the differences in each of the provision of enactment pertaining to the financial reporting.

To some extent, those who intend to further investigate the financial reporting should read this study with caution. This study has been done in the year 2000. The information might differ as time passes by, where various new legislation and enactment might be issued by the SIRCs.

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